

## **Tax Working Group Public Submissions Information Release**

### **Release Document**

**September 2018**

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In preparing this Information Release, the Treasury has considered the public interest considerations in section 9(1) of the Official Information Act.



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## **SUBMISSION**

To  
**Tax Working Group Secretariat**

PO Box 3724  
Wellington 6140  
New Zealand

[submissions@taxworkinggroup.govt.nz](mailto:submissions@taxworkinggroup.govt.nz)  
on

## **FUTURE OF TAX**

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Date: 30<sup>th</sup> April 2018

Contact: Greg Sneath  
Organisation: The Fertiliser Association of New Zealand  
Postal Address: PO Box 11519, Manners St, Wellington, 6142  
Phone: (04) 473 6552  
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## **About Fertiliser Association of New Zealand (FANZ)**

- 1 FANZ is a trade association representing the New Zealand manufacturers of superphosphate and nitrogen fertilisers. FANZ member companies are Ballance Agri-Nutrients Ltd and Ravensdown Limited. Both these companies are farmer co-operatives with some 45,000 farmer shareholders, and between them supply over 98% of all fertiliser used in New Zealand.
- 2 The cooperative base of the fertiliser industry means the industry is driven by delivering best value to its farmer shareholders. The industry is focussed on fertiliser effectiveness and efficiency enabling profitable farming operating within environmental limits.
- 3 FANZ on behalf of the industry supports and encourages an environmentally responsible, science-based approach to nutrient management and regulation.
- 4 FANZ member companies provide product that is critical to New Zealand farming systems with interests and responsibility across all agricultural sectors, including dairy, sheep, beef, arable and horticulture. The industry has an almost unique pan-sector perspective.
- 5 To promote good management practices, FANZ has funded training programmes, and developed codes of practice, information booklets and fact sheets. FANZ also funds research, partners with government on research and development projects, and works closely with other organisations in the agricultural sector on industry-good issues. Along with AgResearch and the Ministry for Primary Industries, FANZ is a part owner of OVERSEER®. OVERSEER is discussed in the body of this submission. It is an agricultural management tool which assists farmers and their advisers to examine nutrient use and movements within a farm system. (see appendix A for background information on OVERSEER)

### **FANZ's philosophy and approach**

- 6 The industry supports systems that provide flexibility for land users to achieve desired outcome from an environmental and production perspective by managing farm system losses. This allows farmers to choose the most effective way of achieving outcomes for their particular property. It helps avoid regulation un-intentionally constraining business growth and allows for flexibility, innovation and transition to achieve both primary production goals and environmental outcomes.
- 7 In an environmental context FANZ supports 'effects' based measures as prescribed under the RMA. Effects in this context result from the losses from the farm system. Many losses cannot be measured directly. In the absence of direct measurement, modelling approaches can be used for management of effects. The model OVERSEER estimates a farm system's annual average inputs and outputs of nutrients per hectare per year.

- 8 This Fertiliser Association of New Zealand (FANZ) submission on The Future of Tax primarily addresses issues relating to tax considerations as they apply to agricultural emissions and nutrient management.

### **Executive summary**

- 9 Taxes are accepted for the purpose of revenue gathering and/or to drive behaviour.
- 10 Environmentally focussed taxes are considered to have the primary purpose of driving behaviour leading to favourable environmental outcomes. A secondary purpose could be raising revenue to deal with negative externalities or to support investment in innovation.
- 11 In the context of an environmentally focussed tax, key considerations for a national tax are to avoid a blunt ineffective tool and provide for flexibility and innovation to address locally diverse impacts on the environment, while providing for efficient and internationally competitive productivity.

### **Dealing with varied environmental impacts under taxation policy**

- 12 One difficulty in implementation of environmental taxes is due to the complex and varied relationship, between land use activities and impact on natural resources. For an issue such as water quality, the impact will vary catchment by catchment. In one catchment the impact of concern might be bacteriological contamination, in another the issue could be the adverse impact of nutrient, in another sediment load.
- 13 A nationally applied tax system to achieve environmental outcomes under these circumstances, is likely to be inefficient and ineffective.

### **Coherence of taxation policy with other policies**

- 14 A key consideration for an 'environmental' tax policy is that it should be coherent with other government objectives and forms a part of a suite of measures rather than being a blunt stand-alone instrument. This means that as well as being coherent with central government policy, coherence is also needed between any tax regime and local government policies.
- 15 Environmental controls are essentially implemented by regional and district councils under the Resource Management Act, so there is a need to evaluate how central government taxation measures integrate with the wide range of territorial and industry initiatives to target and address local environmental issues.

### **Taxation as a tool for driving behaviour change**

- 16 Driving behaviour change through a taxation approach requires a direct link between behaviour and what being taxed. There are potential risks in using tax alone to drive behaviour. A low tax could prevent a proper focus on mitigations – because it will be cheaper to pay the tax rather than bear the costs of mitigation. A high tax can have a significant impact on national economic productivity and social well-being.
- 17 Nitrogen fertiliser is an essential component of modern farming practices and nitrogen fertiliser use is relatively inelastic to changes in price. Taxation on nitrogen for environmental controls, either as a straight input control or an output-based tax, as proposed by some, are unlikely to effect behaviour change nor deliver any improvements above and beyond existing initiatives in development, including regulatory and non-regulatory controls. A tax on nitrogen would introduce unnecessary complexity and administrative burden to the tax regime for little direct environmental benefit.

### **Taxation targeted at revenue generation**

- 18 Tax can also generate revenue with which to address mitigations, community programmes, compensate for degradation, or allow for government investment in innovation. Administrative efficiency has to be a key consideration in gaining revenue this way. Equally important the tax must be recognised as fair and justified.

### **International competitiveness**

- 19 New Zealand agriculture sells products in a global market so international competitiveness needs to be a consideration. Should New Zealand land-based industries face unique costs which are not borne by their competitors in the international market place? Consideration to ensuring retention of international competitiveness in light of any added tax burden imposed on land users is key, not least because of the primary industry generates more than 50 % of New Zealand' export earnings.
- 20 International (global) greenhouse gas commitments based on absolute limits for emissions must be addressed, however food security considerations and production efficiency consideration require provision for intensity-based measures as part of a suite of options.

### **Can international approaches be translated to a New Zealand context?**

- 21 Examples of fertiliser taxes used internationally cannot be transferred to a New Zealand circumstance because of New Zealand's unique position compared to OECD countries with its reliance on agriculture and its absence of subsidies.

- 22 It is noted and supported that New Zealand's current tax system was rated by US based Tax Foundation in 2017, as second in the world for competitiveness. The Foundation states that the taxation system was changed in 2010 in response to trends where New Zealand was losing its international competitiveness. By this measure New Zealand may be deemed to be in a favourable position overall under the current tax system, requiring only adjustment of the components of which the overall rating is comprised.

### **Principled based approach to taxation**

- 23 The Fertiliser Association supports the principles that:
- Tax systems should avoid complexity
  - Tax systems must be seen as fair and equitable
  - Tax systems achieve or drive desired outcomes
- 24 And to ensure economic and social well-being for New Zealand, a tax for revenue collection or behaviour change should:
- operate neutrally and as much in the background as possible, (meaning impose as little distortion on economic decisions as possible), and,
  - retain as much international competitiveness as possible
- 25 These very broad principles are consistent with the Government's stated principles and objectives for tax which are articulated in the Terms of Reference for the Tax Working Group.
- 26 Taxes that might apply to environmental outcomes and agricultural production, is the focus of this submission.

### **Submission**

- 27 In the recent past discussions, environmental tax has been proposed in the form of taxes on:
- nitrogen fertiliser input; nitrogen leaching losses; greenhouse gas losses.
- 28 Other taxes impacting on agricultural production may include:
- land tax, resource rental tax, water take or water use tax

## Environmental Taxes – Nitrogen

29 Nitrates are raised in the discussion in the Future of Tax Submissions Background Paper under environmental considerations, in relation to monitored water sites in New Zealand.

30 The paper states;

*“Nitrate levels have generally worsened at monitored water sites, although phosphorous levels have improved”*

31 To address the issue effectively, it is important to understand the context of this statement. Ministry for the Environment and Statistics New Zealand report, “*Our fresh water 2017*” notes (page 7), that:

*“The water quality information largely comes from regional and unitary councils, NIWA, and GNS monitoring networks. For the regional council networks in particular, many monitored sites tend to be in areas of known, or suspected, issues so that regional councils can make management decisions; however, this potentially leads to a biased view of national water quality. To overcome this issue, we used modelled water quality data to estimate water quality in areas where we do not have data. We also use models to estimate nitrate leaching and periphyton growth, to help us build the story around water quality pressures and impacts. We currently have limited data on the pressures and impacts related to water quality, particularly monitored data at a national scale.”*

32 and states (page 10);

*“However, the trends for nitrate-nitrogen and dissolved reactive phosphorus vary across the country. For some monitored sites, nitrate nitrogen concentrations were improving and dissolved reactive phosphorus concentrations were worsening. For some sites we could not determine a trend direction.”*

33 The Fertiliser Association would argue that it is very clear that the management of nitrogen and phosphorus levels in New Zealand waterways, is a complex issue, which varies by catchment and land use, soil type, terrain and climate.

34 Therefore, nitrate and phosphate losses are unlikely to be successfully managed by a blunt tax instrument applied a national level. It would not be efficient or effective.

35 The drivers of water quality deterioration are different in different catchments. A national level tax would not be able to be proportionate to the impacts in different catchments which vary enormously. To be fair and equitable, such a system would, by necessity, be very complex and cumbersome and would not readily meet the criteria listed in the Principles of a Good Tax System as described in the Future of Tax submissions background document.

- 36 The Resource Management Act (RMA) requires controls to avoid, remedy or mitigate the adverse effects of activities on the environment for the purpose of sustainable management of natural resources.
- 37 The RMA is an effects-based statute which addresses activities that have the potential to cause adverse effects on the environment. In respect to water quality it is not just nutrient losses from activities, but also sediment and microbial contaminant losses which give rise to the adverse water quality effects. Managing losses from these activities on productive land is particularly important in the New Zealand context, because New Zealand is unique amongst OECD countries due to its reliance on the primary industries for its export income and to support our economy and our standard of living.
- 38 An output, (effects-based) control, addressing catchment specific conditions provides flexibility for primary sector to develop innovative solutions to address the losses, while maintaining productivity to support our economy. An effects-based approach can be tailored to meet the appropriate standards for different catchments and communities. (e.g. Appropriate water quality standards and limits for productive lowland pasture will differ to those for productive tussock or steep hill country regions. Nitrogen losses in a sub-catchment of a shallow lake will have very different environmental implications to the same losses in a sub-catchment of a river system near the coast).
- 39 A nationally applied tax system on nitrogen inputs, or even nitrogen losses, will not provide an effective outcome for environmental management across New Zealand.
- 40 The regional council approach under the RMA generally gives effect to the knowledge that nitrogen losses from the farm system come from multiple sources, and generally recognises that direct losses from fertiliser are one, relatively small component, compared to the overall system losses from pastoral agriculture<sup>i</sup>.
- 41 In pastoral agriculture nitrogen fertiliser is principally used strategically to fill feed gaps. Nitrogen fertiliser provides for increased pasture growth, and therefore provides an alternative to importing more expensive supplementary feeds into the farm systems. This strategic input is particularly important for dairy farms at times of low commodity prices. It is important to recognise also that in the absence of nitrogen fertilisers, supplementary feed also introduces nitrogen into the farm system. As stated above, it is recognised that most nitrogen loss from a pastoral farm system is driven by livestock urine deposits, not the fertiliser inputs themselves.
- 42 A tax to address all nitrogen inputs (e.g. clover fixed nitrogen, supplementary feed and fertiliser) would be even more cumbersome, inefficient and inequitable than a tax on nitrogen fertiliser alone.

- 43 Furthermore, for most farm systems the fertiliser cost is the single biggest farm expense, (excluding labour, and for some dairy farms, feed supplements). There is already a strong financial incentive to use these products effectively and efficiently. Accountability for nutrient use has been redoubled with regional council regulation being introduced in most intensive farming areas, which is requiring the reduction of nitrogen losses from the farm systems.
- 44 Fertilisers are an essential component of modern farming. Where there is a tax imposed on essential inputs, the taxation may be viewed as a revenue collecting exercise rather than specifically addressing behaviour change.
- 45 Recent history of the relatively inelastic nature of nitrogen fertiliser use in response to price, is demonstrated when considering average change in urea prices in New Zealand from one year to the next, relative to the annual estimate of total nitrogen use in New Zealand, (Figure 1).
- 46 Using industry estimates, Figure 1 shows clearly that despite some occasions with reduced nitrogen fertiliser use at times of increased price, there are also many times of significant increase in urea fertiliser price where the annual nitrogen fertiliser use has remained relatively static or marginally increased. And there are several examples showing a reduction in nitrogen use, regardless of a fall in the price of urea.
- 47 The relatively inelastic nature of nitrogen fertiliser use in New Zealand in response to price, means that any tax imposed to drive behaviour change would have to be so significant it would have a detrimental effect on the agriculture productivity and international competitiveness of our primary industry. (Tax on petrol provides a good example of a tax on an essential input where demand and use is relatively inelastic to price, and therefore a tax to drive behaviour change would have to be so high, it would risk significant economic impacts)

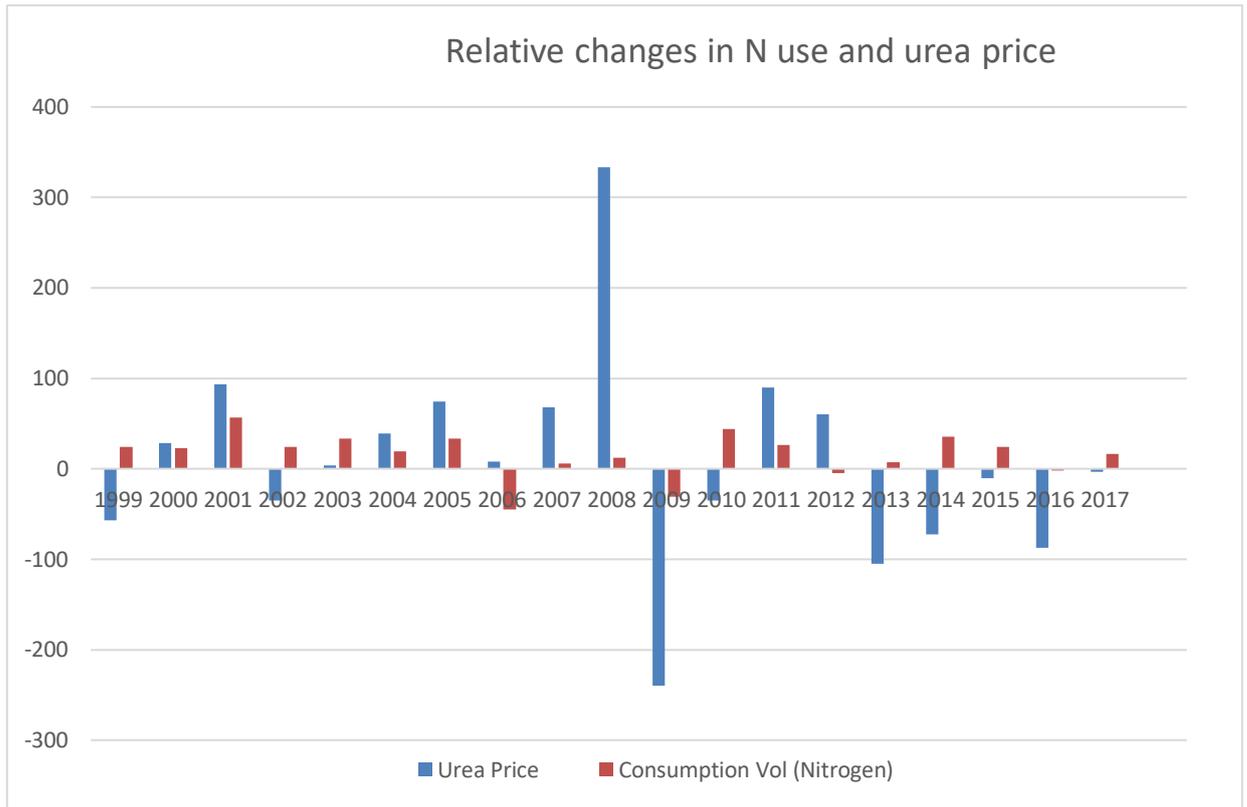


Figure 1 : Relative changes in average urea price compared to changes in estimated national nitrogen consumption

- 48 Several international reports, in particular from Europe, address taxes on nitrogen fertiliser inputs to achieve environmental benefits. In general, these reports confirm some reduction on fertiliser use as a result of tax, however, the circumstances are not directly applicable to New Zealand because of the subsidies provided for farms. Furthermore, the application of environmental tax has only been one part the approach, which is also reliant on significant investment in education and extension support.
- 49 In some countries the fertiliser tax revenue was used to subsidise agricultural exports. In some European countries, (e.g. Finland and Austria) where significant fertiliser taxes were introduced, these were later abolished<sup>ii</sup>.
- 50 Therefore, for a combination of reasons, a tax system on nitrogen inputs as applied to European agricultural settings is not comparable to the New Zealand economic circumstance where there are no subsidies and there is full exposure to economic signals.
- 51 Through industry programmes and regional council approaches to managing water quality there are already a number of regulatory and non-regulatory controls which limit nitrogen losses. There are a number of regional council and industry- based education programmes targeting improved farm systems and environmental accountability.

52 Introducing a blunt nitrogen fertiliser tax to achieve similar initiatives would be at best, unnecessary, and at worst, counterproductive, as a tax would be unlikely to drive behaviour change beyond what is being achieved by current programmes, and would impose a cost on what is an essential component of many farm systems, as demonstrated by the relative inelasticity to price.

#### OVERSEER®

53 Many regulatory controls being implemented by regional councils to address nitrogen losses to freshwater bodies recognise the importance of providing for economically viable agricultural production with flexibility to respond to market forces and to adopt innovative solutions. Measuring these farm system losses is prohibitively expensive so a modelling approach has been adopted. OVERSEER Nutrient Budget model has been recognised as the best available tool and has been incorporated into regulation in many regional councils.

54 The election manifesto of the Green Party clearly recognises the value of OVERSEER Nutrient Budget model, but has recommended a tax based on nitrogen losses modelled using OVERSEER.

55 While this approach of taxing farm system losses is consistent with an effects-based approach supported by the fertiliser industry, the industry is opposed to this taxation for several reasons.

56 In the first instance, the effects-based limits on nitrogen loss are being developed under Resource Management Act legislation and further significant farm system change is anticipated under the soon to be developed climate change mitigation requirements. If an output tax is applied on top of the costs for farm system changes, or on top of the additional production costs and new investments required by the primary industry to meet nutrient loss limits to achieve these environmental targets, then the proposed tax becomes a punitive taxation measure with no benefit other than to gather revenue.

57 It is proposed by the Green Party that the tax revenue will be targeted to environmental programmes (reinvested to 'sustainable farming') however, the cost of RMA compliance will be very significant for many farms, driving adaptation and change. Adaptation and change will be expensive and difficult to sustain under existing legislation. An additional tax burden on nutrient loss which meets obligations under the RMA, will very likely have significant impact on the economic viability of the primary industry.

58 Such an approach could not be seen as fair and equitable, because it imposes a 'double whammy' of costs on the producers already obliged by legislation to achieve environmental limits.

- 59 The proposed tax burden based on output limits using OVERSEER Nutrient Budgets faces an additional obstacle if the nature of modelling at farm system level is well understood.
- 60 The OVERSEER Nutrient Budget model is a long-term, annual average model used to understand nutrient cycling in a farm system. It assumes the farm system is in equilibrium and not undergoing change. The model cannot measure nutrient losses, but provides for a benchmark and an estimate based on the farm management system.
- 61 The model can be run using information that is owned by the farmer or easily accessed by the farmer. As the model has become more sophisticated, it requires, particularly if applied for regulatory purposes, an expert user who understands the model (such as a Certified Nutrient Management Adviser) and applies data following OVERSEER Data Input Standards. This ensures more consistent and reliable use of the model, and minimises differences arising from different operators. The model represents the best available science and is updated as new science and information becomes available.
- 62 Updates and introduction of new science inevitably introduce changes to the results of the model. The impact of these version changes have yet to be fully addressed in those regional plans which rely on a constant absolute value for nitrogen loss for the regulation. For most regulatory applications, the consequence of the version change is to alter the activity status and consent requirements. Because OVERSEER provides a benchmark against which relative change is estimated these regulatory consequences of the OVERSEER version change can be managed, albeit through some difficulty.
- 63 It is not at all clear how a taxation (direct financial obligation) based on a modelled N loss, expressed as an absolute value, can be managed fairly and equitably if difference in N loss estimates occur with each version change.
- 64 Under the principles which apply to taxation – it introduces an extra layer of complexity to taxation, is not fair and equitable and is unlikely on its own to drive behaviour change, particularly if Regional Council regulatory limits already apply.
- 65 If primary industry is already investing heavily in developing improved sustainable systems then, rather than impose an addition burden of cost on the primary sector alone, any further investment for sustainable primary production should be supported by the wider community which benefits from the commerce.

### **Environmental Taxes – Greenhouse Gases**

- 66 New Zealand has a unique profile amongst OECD countries in relation to greenhouse gas emissions due to its reliance on the primary industry sector for export income and due to the fact that agricultural emissions account for almost 50 % of New Zealand GHG emissions. New

Zealand already has 85 % renewable energy resources. This means there are currently few mitigation options readily available to quickly reduce greenhouse gas emissions.

- 67 Agricultural GHG emissions are predominantly from enteric methane (approximately 75%) and then nitrous oxide (approx.15%) associated with livestock. Only a very small percentage of the agricultural emissions are attributed to fertiliser (approx. 4%) and lime (approx. 3%), with the remainder coming mostly from cropping systems.
- 68 It is considered that the government's commitment to the Paris Agreement will inevitably require agricultural emissions to be accounted for and reduced. The mechanism to achieve this is yet to be developed by government policy, and while a carbon tax could be straight forward, it is not easily applied to agricultural settings if the outcome sought is behaviour change when few mitigations available.
- 69 The fertiliser industry recognises that to effect behaviour change at farm level, some form of accountability is required at farm level.
- 70 It is considered that OVERSEER Nutrient Budget provides for a good farm level of accountability. It models GHG emission using methods consistent with the national inventory and if already being used for managing nitrate losses, GHG accountability at farm scale can be provided for with little to no additional effort.
- 71 Human resources and skill capability (e.g. Certified Nutrient Management Advisers) to deliver OVERSEER Nutrient Budgets for every farm in New Zealand is not currently available and so a pragmatic approach which provides for detailed assessment of mitigation for more intensive farm systems using OVERSEER and a parallel, complementary system for less intensive farms with few mitigations available may be required.
- 72 A simple carbon tax and variation of an Emissions Trading Scheme have scope for addressing greenhouse gas emissions at farm scale.
- 73 A carbon tax imposes a price on the unit output. Where it is cheaper to pay the tax, there is no incentive to reduce overall outputs. For this reason, and if seeking maximum efficiency in emissions reductions, a carbon tax remains a crude instrument, unlikely to be effective in addressing agricultural emissions where mitigations are limited. It is likely to be most effective where mitigations or alternatives exist or can be readily developed.
- 74 An emissions trading system approach, places a cap on the unit outputs, and issues permits which can be traded. It provides an opportunity for control of outputs in absolute terms, and signals for reductions required over longer timeframes. It provides for market-based decisions on the most efficient use of the limited allocations.

- 75 The system employed must adhere to the fundamental principles of:
- Driving behaviour change
  - Avoiding complexity
  - Being seen as fair and equitable
  - Apply readily measured and well-defined units.
- 76 International (global) greenhouse gas commitments based on absolute limits for emissions must be addressed, however food security considerations and production efficiency consideration require provision for intensity-based measures as part of a suite of options.
- 77 Use of revenue should be applied with transparency and clarity to ensure it is seen as fair and appropriate to address international obligations and climate change objectives. This could include meeting international obligations through investment in mitigation offsets or investment in locally based climate change mitigations or climate change solutions.

#### **Environmental Taxes – Behaviour change**

- 78 Environmental taxes should ultimately drive behaviour change – but as discussed above, can have positive or negative effects. A low tax could prevent a proper focus on mitigations – because it will be cheaper to pay the tax rather than bear the costs of mitigation. A high tax will have impact on economic productivity and social well-being.
- 79 A key principle is that tax policy is coherent with other government objectives – is part of a suite of measures rather than a stand-alone instrument.
- 80 There could be difficulty in the implementation of national environmental taxes in NZ because many environmental controls are essentially set by regional and district councils – so there is a need to think about how central government taxation measures integrate with regions council initiatives.

#### **Environmental Taxes – Land tax, resource rental tax, water take tax.**

- 81 Other taxes impacting on agricultural production may include land tax, resource rental tax, water take or water use tax.
- 82 These 'other' taxes are not specific to addressing nutrient management issues, but are related to nutrient management if they are proposed to drive efficient use of resources or to reduce adverse environmental impacts while providing for a competitive rural economic economy.
- 83 Many of the considerations discussed under the nutrient issues will apply. Resource rental or land tax are likely to add cost and complexity to the tax system both for administration and for

compliance. This could impact on international competitiveness, but is unlikely to effectively address the environmental impact of land use activities.

84 Revenue gained could be invested in mitigation options and development programmes, however, there is also an argument that the wider community which benefits from the primary industry should also contribute to these schemes, not just this businesses to which land tax, or resource rental tax might be applied.

85 With more than 50 % of New Zealand export income generated by primary industry, maintaining international competitiveness is essential. An added tax burden on rural communities may adversely affect this competitiveness.

86 The Principles of Resource Rentals as described by B.C. Land<sup>iii</sup>, discusses circumstances which are primarily applied to extractive industries rather than primary sector production involving multiple land use activities. However, under 'lessons learned', the paper concludes:

*“Government appetite to take fiscal risk and bear administrative costs depends in part on the scale of revenue at stake and availability of resources to achieve effective administration. This factor would seem to go some way to explaining why Resource Rental Tax has featured more prominently in the oil industry than in the mining industry. (where key determinants impacting on resource rent potential are more complicated, e.g. key determinants of quality are ore tonnages, mineral grades, rate of recovery of ore from a deposit taking into account dilution, the efficiency of ore extraction methods and the efficiency with which a saleable mineral product is obtained from the ore.)*

87 International experience has, in several circumstances, shown that complexity and high administrative costs typically associated with resource rental tax, significantly erode the anticipated revenue where resource rental taxes have been introduced.

88 In consideration of the discussion points raised by Land in relation to resource rentals, it seems unlikely that the balance of revenue measured against administration complexity and fiscal risk would be favourable when weighed against requirements of resource rental tax for complicated and varied land-use activities.

89 Environmental gains and effective management of land use activities are likely to be more effective and efficient through working with industry programmes, combined with existing regulatory and non-regulatory approaches under the RMA. Flexibility for land users to adapt and respond to market pressures remains essential, provided the farm system losses which impact on environmental bottom line are accounted for and controlled. It is unlikely these outcomes will be achieved effectively by a broad, national application of resource rental tax to address a variety of land use activities.

- 90 Land taxes and water taxes provide an opportunity for revenue collection for community programmes - however, a direct fiscal risk applies where the tax requires a balance between opportunity for revenue collection and enabling economic viability and competitiveness for the wide range of land-use activities to which these taxes will apply. These considerations must apply also during cycles of economic downturn. As with resource rental tax, benefits of revenue collection and behaviour change would need to be weighed against administrative and fiscal risks.
- 91 If the driver is for improved environmental outcomes, then as with previous discussion, the Fertiliser Association considers a crude national tax approach will be less effective than industry programmes working with a mix of regulatory and non-regulatory initiatives targeting specific environmental outcomes for regional localities. Indeed, these approaches will be required to give direction and to assist and support land-use managers, regardless of the tax regime imposed.
- 92 The effectiveness of the approach and the effects of a double whammy of costs imposed on land-use managers by these other land or resource taxes must be considered in light of international competitiveness.

# Specific questions in the Future Tax Submissions Background Paper.

## Chapter 2: The future environment

What do you see as the main risks, challenges, and opportunities for the tax system over the medium- to long-term? Which of these are most important? How should the tax system change in response to the risks, challenges, and opportunities you have identified? How could tikanga Māori (in particular manaakitanga, whanaungatanga, and kaitiakitanga) help create a more future-focussed tax system?

## Chapter 3: Purposes and principles of a good tax system

### Principles for assessment

What principles would you use to assess the performance of the tax system?

93 Comment:

A good tax system must:

Achieve its intended purpose, (drive intended behaviour change, raise revenue)

Avoid unintended consequence

Remain relatively neutral to market signals for productive agriculture,

Ensure international competitiveness, and generation of wealth

Avoid complexity, for administrative efficiency and ease of application

Be seen as fair and equitable

Apply readily measured and well-defined units.

### Defining 'fairness'

**How would you define 'fairness' in the context of the tax system? What would a fair tax system look like?**

94 Comment:

A fair tax system (in relation to environmental considerations of nitrogen or phosphorus losses to address water quality, and greenhouse gas emissions to address climate change) would enable primary sector producers to respond with appropriate management practices to improve

efficiencies, while meeting both environmental limits and market demands for international competitiveness.

A fair tax would be seen as necessary as well as effective: without imposing unnecessary additional costs which do not have clear relationship to the objectives of the tax.

Provide for past investments, infrastructure and development in land-use activities without undue penalty and provide for suitable transition for businesses to respond to taxation and market signals.

Provide for consistent and stable business operating environment, e.g. long-term signals to changes in cost structures to protect business from sudden price shock. (That is, provide for business confidence and stability in long term planning and investment.)

## Chapter 4: The current New Zealand tax system

### Frameworks

New Zealand's 'broad-based, low-rate' system, with few exemptions for GST and income tax, has been in place for over thirty years. Looking to the future, is it still the best approach for New Zealand? If not, what approach should replace it?

95      Comment:

New Zealand's current tax system was rated by US based Tax Foundation in 2017<sup>iv</sup>, as second in the world for competitiveness. The Foundation states that the change in taxation system was introduced in 2010 in response to trends where New Zealand was losing its international competitiveness. By the measures of the Tax Foundation competitiveness has been retained.

By this measure New Zealand may be deemed to be in a favourable position overall, perhaps requiring only adjustment of the components of which the overall rating is comprised.

### Taxes and behaviour

Should there be a greater role in the tax system for taxes that intentionally modify behaviour? If so, which behaviours and/or what type of taxes?

96      Comment:

Taxes to modify behaviour require a direct relationship between the product cost and behaviour.

Tax on commodities or resources which are inelastic to price are unlikely to achieve behaviour change outcomes until the tax is sufficiently high that it will have negative social or economic effects. (e.g. increasing tax on petrol, may change driving behaviour and reduce fuel consumption only for a short period as a direct response to price.)

Taxes designed to drive behaviour change, require that mitigation options are available for a specific activity, or that the activity should cease entirely. The latter introduces fiscal, administrative and social risks.

Where options for behaviour change are limited, tax incentives may play a more powerful role, than an increased cost burden from tax on businesses.

### Retirement savings

Should the tax system encourage saving for retirement as a goal in its own right? If so, what changes would you suggest to achieve this goal?

## Chapter 5: The results of the current tax system

### Fairness and balance

Does the tax system strike the right balance between supporting the productive economy and the speculative economy? If it does not, what would need to change to achieve a better balance?

97 Comment:

New Zealand's current tax system has a very broad and even base compared to many international tax systems. It was rated by US based Tax Foundation in 2017, as second in the world for competitiveness. The Foundation states that the taxation system was changed in 2010 in response to trends where New Zealand was losing its international competitiveness.

By this measure New Zealand may be deemed to be in a favourable position overall, requiring only adjustment of the components of which the overall rating is comprised.

By this measure of competitiveness and neutrality- A competitive tax code is one that keeps marginal tax rates low, and neutrality seeks to raise the most revenue with the fewest economic distortions.

## Tax and business

Does the tax system do enough to minimise costs on business?

98 Comment:

The US Based Tax Foundation ranked New Zealand as 2<sup>nd</sup> overall for competitiveness amongst OECD countries.

Does the tax system do enough to maintain natural capital?

99 Comment:

Natural capital of land use cannot be efficiently addressed by a national, centrally driven signal when natural capital for primary production is highly variable and influenced by natural resources of climate, soil type, terrain, access to water etc. It will require a complex and cumbersome tax system to effectively address natural capital at a national level. Better management through a mix of regulation, industry good programmes, and market assurance programmes will be necessary, as it is most unlikely a taxation based on natural capital can address the myriad of issues natural capital introduces to land use activities and business opportunities.

Are there types of businesses benefiting from low effective tax rates because of excessive deductions, timing of deductions or non-taxation of certain types of income?

100 Comment:

To remain competitive, New Zealand has implemented a relatively simple tax system, which is easy to understand and apply, limiting administration costs. Top marginal individual income tax rate were lowered to 33 percent, corporate tax rate reduced to 28 percent with increased of reliance on the goods and services tax for revenue. The USA based Tax Foundation also notes further competitive characteristics of the existing scheme as including, no inheritance tax, no general capital gains tax, and no payroll taxes. By this assessment New Zealand has generally low rates but high revenues compared with other OECD countries

It may be expected that New Zealand businesses and the New Zealand economy are benefiting from a high degree of relative international competitiveness.

## Chapter 6: Thinking outside the current system

What are the main inconsistencies in the current tax system? Which of these inconsistencies are most important to address?

Is there a case to consider the introduction of any new taxes that are not currently levied? Should any taxes be reduced if new taxes are introduced?

## Chapter 7: Specific challenges

### Housing affordability

How, and to what extent, does the tax system affect housing affordability for owners and renters? Is there a case to change the tax system to promote greater housing affordability? If so, what changes would you recommend?

### Capital gains tax

Should New Zealand introduce a capital gains tax (that excludes the family home)? If so, what features should it have?

### Land tax

Should New Zealand introduce a land tax (that excludes the land under the family home)? If so, what features should it have?

101 Comment:

As discussed in the submission, land tax alone, if applied to the rural environment, is unlikely to effectively address the environmental impact of land use activities. It would add cost and is likely to impact negatively on international competitiveness, as well as add complexity to the tax system. Revenue gained could be invested in mitigation options and development programmes, however, there is also an argument that the wider community which benefits from the primary industry should also contribute, not just this businesses to which land tax, or resource rental tax might be applied. With more than 50 % of New Zealand export income generated by primary industry, maintaining international competitiveness is essential and land tax introduces the potential to adversely affect this competitiveness at a time when regional regulation and controls are currently imposing a very significant burden on many primary industry businesses to achieve environmental outcomes. For these reasons a land tax should not apply to rural production land or the associated land necessary for supporting infrastructure and services.

### Environmental taxation

What are the main opportunities for effective environmental taxation?

102 Comment:

A form of carbon tax, or Emission Trading Scheme provides for a nationally consistent approach to address the limits required for greenhouse gas emissions. The effects of these emission are felt at not just a national scale, but global scale. Therefore there is opportunity to provide for mechanisms addressing both a cap in emissions and supporting improved efficiency in production of food, for increased food security, using intensity-based measures.

A national taxation instrument to address local water quality issues will be cumbersome, inefficient and ineffective in comparison to other measures which can account for the highly variable nature of the local uses. These include working with industry programmes and a combination of regulatory and non-regulatory methods.

### Progressive company tax

Should the tax system do more to support small businesses? In particular, is there a case for a progressive company tax?

### GST exemptions for particular goods

Should the tax system exclude some goods and services from GST? If so, what should be excluded?  
What else should be taxed to make up for the lost revenue

## Concluding comment

103 Thank you for the opportunity to present this feedback and comment on the 'Future of Tax'.

[1]

Greg Sneath

Executive Manager

The Fertiliser Association of New Zealand

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<sup>i</sup> *Over the last twenty years, sales of nitrogen fertiliser have increased steeply. But while some nitrogen entering waterways will have come from nitrogen fertiliser, this fertiliser is a much smaller source of nitrogen than animal urine. However, the increased use of urea fertiliser has, along with irrigation and supplementary feed, enabled higher stocking rates, and more animals mean more urine.*  
(Parliamentary Commissioner for the Environment, Water quality in New Zealand: Land use and nutrient pollution, (November 2013))

<sup>ii</sup> Study on Environmental Taxes and Charges in the EU, ECOTEC in association with CESAM, CLM, University of Gothenburg, 2001. (pages 150, 382)

<sup>iii</sup> Resource Rent Taxation – Theory and Experience, Bryan C. Land, September 22, 2008

<sup>iv</sup> <https://taxfoundation.org/2017-international-tax-competitiveness-index/>

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## Appendix A

### **OVERSEER®**

- 1 OVERSEER is an agricultural management tool which assists farmers and their advisers to examine nutrient use and movements within a farm system. It assists in decision making for nutrient use to optimise production and manage the risk of losses to the environment. It is a science-based model that is regularly updated to incorporate improved science.
- 2 OVERSEER provides a long-term annual average estimate of nutrient cycling in a farm system. It does not provide for day to day management, but rather provides estimates for each of the pathways for nutrient sources and losses for a farm system. It assumes the farm system is in a stable state and not undergoing transition from one system to another, or from one level of development to another.
- 3 These diffuse nutrient losses from farm systems cannot easily be measured. Modelling provides estimates of these nutrient movements and can be used to understand nutrient requirements to maintain soil fertility at its current levels, and also, to understand the relative change in nutrient losses under different scenarios for a farm system. (Nutrient losses include outputs to saleable product, to the atmosphere or to surface runoff and leaching below the root zone).
- 4 Use of OVERSEER for critical evaluations, such as for regulation, requires qualified and experienced advisers who have a good understanding of the model's operations and underlying assumptions. It also requires standardised data inputs and a good understanding of farm systems and nutrient management.
- 5 Use of OVERSEER has required significant development of capability in farm advisers.

### **Nutrient Management Adviser Certification Programme**

- 6 The Nutrient Management Adviser Certification Programme (NMACP) was developed with the aim of building and upholding a transparent set of standards for nutrient management advisers to meet, so that they provide nationally consistent advice of the highest standard to farmers.
- 7 There are currently over 172 certified nutrient management advisers throughout New Zealand.